STATE OF CALIFORNIA

GRAY DAVIS, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

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August 5, 1999

VIA UNITED PARCEL SERVICE AND ECFS

Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, D.C. 20024

Re: CC Docket No. 96-45
CC Docket No. 96-262

Dear Ms. Salas:

Please find enclosed for filing an original and twelve copies of the "REPLY COMMENTS OF THE PEOPLE OF THE STATE OF CALIFORNIA AND THE CALIFORNIA PUBLIC UTILITIES COMMISSION" in the above-referenced docket. Also enclosed is one additional copy of this document. Kindly file-stamp this copy and return it to me in the enclosed self-addressed envelope.

California is also providing an electronic copy of these comments via your ECFS system.

Thank you for your attention to this matter. If you have any questions, I can be reached at (415) 703-2047.

Sincerely,

Ellen S. LeVine

Ellen S. LeVine
Attorney for California

ESL:abh

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BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

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AUG 06 1999

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In the Matter of Federal-State Joint Board on Universal Service	CC Docket No. 96-45
Access Charge Reform	CC Docket No. 96-262

REPLY COMMENTS OF THE PEOPLE OF THE STATE OF CALIFORNIA AND THE CALIFORNIA PUBLIC UTILITIES COMMISSION

The People of the State of California and the California Public Utilities Commission ("California") hereby file this response to initial comments on the Further Notice of Proposed Rulemaking ("FNPRM") issued by the Federal Communications Commission ("FCC") in its universal service proceeding referenced above.

As recognized by both Congress and the FCC, the purpose of universal service is to ensure that primarily residential customers have access to affordable telephone service. Towards this end, California has urged the FCC to adopt a federal universal service support methodology which establishes variable funding levels which specifically target support to truly high cost areas to ensure affordable service. California supports the FCC's proposed variable support methodology, which provides a lower percentage of cost support in study areas in which costs are slightly above the national average, and an increasing percentage of support in study areas in which costs exceed the national average.

At the same time, California urges the FCC to adopt a methodology that equitably balances consumer interests in those states which are contributors to, and in those states which are recipients of, federal funding. California agrees with the FCC that a methodology that produces a federal fund at or near existing level produces affordable rates, balances the interests of contributor and recipient states, and thus satisfies the goal of universal service.

I. The FCC Should Reject Proposals That Significantly Expand The Size Of The Federal Fund Above The Current Level

It bears emphasis that modifications to the federal high cost fund mechansims adopted in this phase are precedential. Any proposals that greatly increase the size of the fund which are adopted in this phase will undoubtedly be considered in the phase addressing the high cost fund reform of rural carriers as well. Thus, the decisions made in this phase will have compounding effects when applied to rural carriers.

Certain parties, including a coalition of states calling themselves "Commenting Non-Urban State Commissions," have offered proposals that would dramatically inflate the size of the federal fund beyond its current level. For example, the Commenting Non-Urban State Commissions propose a methodology that would produce a subsidy requirement of $5.61 billion, with $3.14 billion funded at the federal level. The $3.14 billion funding requirement does not include additional funding needed to support a hold-harmless provision.[1] This amount, without hold-harmless support, is over fifteen times the current level of federal funding.[2] While no doubt such a proposal is greatly beneficial to the states represented by Commenting Non-Urban State Commissions, it requires large, urban states, like California, Illinois, New Jersey, and New York, to subsidize other states in amounts well in excess of their current contributions to the federal fund. At the same time, none of the non-rural carriers within these urban states will receive any federal funding.[3] The amount of federal funding proposed by the non-urban states is excessive, produces inequitable results, and should not be adopted.

The Commenting Non-Urban State Commissions further propose, in satisfying the reasonable comparability standard of Section 254(b)(3), that rural rates be no greater than 125 percent of urban rates, both within and among states. Under this proposal, to the extent that this rate differential is not maintained, federal universal service support would be provided to achieve it. To justify this modest rate differential, the Commenting Non-Urban State Commissions believe that the rate comparability standard is designed to ensure that rural rates promote rural economic development.[4] Rural economic development, however, is not, nor should it be, the purpose of urban/rural rate comparability. To the contrary, urban/rural rate comparability is designed to ensure that residential customers have access to affordable telephone service. It is not designed to

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1 Commenting Non-Urban State Commissions at 14.

2 Cincinnati Bell Telephone Company Comments at 3 (current level of non-rural support is about $220 million.)

3 Commenting Non-Urban State Commissions, Exhibit A, Schedules III and IV.

4 Commenting Non-Urban State Commissions at 15.

require consumers in urban states to subsidize rural states for the purpose of spurring rural economic development.

In addition, as California and others have commented, the responsibility for ensuring comparability between rural and urban rates is primarily a state matter, and is not a responsibility that other states should be required to assume. [5] In California, carriers are eligible to receive explicit subsidy support for residential high cost areas that exceed 150 percent of the statewide average residential cost of $20.30. The 150 percent standard has been in place for California's small local exchange carriers for more than ten years, and has successfully yielded urban/rural rate comparability that ensures affordable access to basic telephone service for all of California's residential ratepayers.

In contrast to California's universal service program, the non-urban states' proposal for a federal program, using a 125 percent benchmark, would require California consumers to subsidize out-of-state access lines by an additional $3.37 beyond the level at which they underwrite access lines within California.[6] And, for illustrative purposes only, California estimates that the use of a 150 percent comparability standard would require a federal funding level of approximately $1.5 billion -- nearly a sevenfold increase

[5] California Comments at 2 ("the federal methodology should rely primarily on states to achieve reasonably comparable rates between urban and high cost areas within their borders, while providing federal support for states with above-average costs to the extent that such costs prevent the state from ensuring such comparability.")

[6] The $3.37 differential is derived as follows using the assumptions made by Commenting Non-Urban State Commission (Exhibit A): $19.57 Pacific Bell statewide average cost, times 79.67% "Urban Rate Factor" = $15.59, times 74% intrastate factor = $11.54, times 150% benchmark factor used by California High Cost Fund = $17.32 maximum comparable California rate, minus maximum rate proposed by Commenting Non-Urban States of $13.87 = difference of $3.37.

over the current funding level. In short, the non-urban states' proposal unduly burdens California consumers, and should not be adopted.

As discussed in our initial comments, in adopting a rate comparability standard, California supports a funding methodology that provides graduated federal support above a reasonable percentage differential between urban and rural rates, and then caps the overall level of support. Such a methodology will help to control the overall size of the fund, and ensure that support is targeted to areas that truly require it. The current mechanism provides maximum support of 75 percent for loop costs that exceed the national average cost by 250 percent. A graduated funding approach similar to that currently in place will ensure that consumers in states, like California, who are already funding state universal service programs, are not saddled with 100 percent of the costs of a federal program beyond the national benchmark.[7]

II. The FCC Should Average The Cost Of Providing Universal Service Over A Study Area

Many large and small states, including California, support a methodology that would average the cost of providing universal service over a study area in determining the

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[7] California ratepayers are currently contributing more than $400 million to the state's high cost funds through an end user surcharge applied to all end user billings of California intrastate telecommunications services.

[8] Commenting Non-Urban State Commissions at 15; New York Public Service Commission Comments at 6; California at 9-14. Accord, AT&T Comments at 12.

level of federal support.[8] By determining the level of federal support at the study area level, the size of the federal fund is minimized and kept within a reasonable level.[9]

At the same time, many states, including California, agree that the distribution of federal support should be at a more granular level, such as at the wire center. [10] Distributing federal support at the wire center level targets high cost support to areas of specific need. California, however, disagrees with those parties who urge the FCC to deaverage federal high cost support to unbundled network element ("UNE) zone levels. Until states have adopted deaveraged UNE rates in particular zones and have had an opportunity to determine the effect of deaveraged wholesale rates on retail rates, it would be premature to assume that the distribution of federal universal service support should be targeted to those same zones.

III. The Federal Methodology Properly Calculates Carrier Contributions On The Basis Of Interstate Revenues, Properly Relies On Forward-Looking Costs, and Properly Requires Wireless Carriers To Contribute To The Federal Universal Service Fund

In its FNPRM, the FCC noted that, in determining the revenue base upon which carriers would contribute to federal universal service, the FCC had declined to assess both interstate and intrastate end-user revenues for the high-cost and low-income support mechanisms. FNPRM, ¶ 87. The FCC also declined to permit carriers to seek recovery

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9 Although SBC does not support using a study area as the basis for determining support levels, SBC does acknowledge that utilization of a study area may provide enough support to achieve reasonable rate comparability among states. SBC Comments at 5.

10 E.g., California Comments at 10; New York Public Service Commission Comments at 6. Accord, AT&T Comments at 13.

of their universal service contributions through intrastate rates. Id. Several parties, however, have urged the FCC to include a carrier's intrastate revenues in determining the level of contribution by carriers, and to permit the recovery of such contribution in both intrastate and interstate rates.

The recent decision by the United States Court of Appeals for the Fifth Circuit in Texas Office of Public Utility Counsel v. FCC, No. 97-60421 (issued July 30, 1999) is dispositive of these issues. There, the Court made clear that the FCC may not lawfully include intrastate revenues in the assessment base for contributions to the high-cost and low-income universal service support mechanism. Slip op. at 36-37. The Court also held that the FCC may not lawfully refer carriers to the states to seek recovery of a portion of their contributions to federal universal service funds. Slip op. at 37-38.

In addition to the above, the Fifth Circuit upheld the FCC's earlier determination that wireless carriers should be required to contribute to state universal service funding. Slip op. at 19. The Court also upheld the FCC's reliance on forward-looking costs in determining a federal funding methodology. Slip op. at 7. Accordingly, the FCC should reject the attempt by some parties which seek to revisit these issues on legal grounds.[11]

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[11] The FCC should also decline to entertain proposals which advocate an entirely different methodology for determining federal universal service support. For example, SBC's methodology, which factors universal service expense as a household expense, and then determines affordability of telephone service on a state-specific basis as determined by household income levels, is unduly complex and administratively burdensome.

Moreover, the policy grounds which supported these prior determinations remain equally valid today.

Respectfully submitted,

PETER ARTH, JR.
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ELLEN S. LEVINE

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August 5, 1999

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the foregoing document to be served upon all known parties of record by mailing, by first-class mail, postage prepaid, a copy thereof properly addressed to each party.

Dated at San Francisco, California, this 5th day of August, 1999.

ELLEN S. LEVINE